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Micro Finance: A Poverty Reduction Tool

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Abstract – Indian population comprises approximately one sixth of the world's population. Among this, ten percent of the population possesses a large proportion of the total wealth of india. Interestingly, during the past few years, Indian has demonstrated a welcome willingness to innovate and to think afresh about financial services to alleviate poverty. The poverty, reduction has become the object of unprecedented attention at national and international level. The dynamic growth of the microfinance industry has been promoted not only by market forces but also by conscious actions of national governments, Non-government organization and the donors who view microfinance as an effective tool for eradicating poverty. Thus the concept of micro finance gained growing recognition as an effective tool in improving the quality of life and living standards of poor people. This paper argues that microfinance can be considered an improvement element for an effective poverty reduction strategy. It shows that access and efficient provision of microcredit can enable the poor to smooth their consumption, manage their risks better, gradually build their assets, develop their micro enterprises, enhance their income earning capacity and enjoy an improved quality of life.

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INTRODUCTION

Microfinance can be a critical element of an effective poverty reduction strategy. Improved access and efficient provision of savings, credit, and insurance facilities enable the poor to smoothen their consumption, manage their risks better, and build their assets gradually and develop their micro enterprises.

Microcredit emphasizes the provision of credit services to low income clients, usually in the form of small loans for micro enterprise and income generating activities. Use of the term 'microcredit' is often associated with an inadequate amount of the value of savings for the poor. In most cases, the provision of savings services in 'microcredit' schemes simply involves the collection of compulsory deposit amounts that are designed only to collateralize those loans. Additional voluntary savings may collect but the clients have restricted access to their enforced savings. These savings become the main source of capital in the financial institutions.

Microfinance sector has growth rapidly over the past few decades. Nobel laureate Muhammand Yunus is credited with laying the foundation of the modern MFI's with establishment of Grameen Bank, Bangladesh in 1976. Today it has evolved into a vibrant industry exhibiting a variety of business models. Microfinance institutions in Indian exist as NGOs, section 25 companies and Non-Banking Financial Companies. Commercial Banks, Regional Rural Banks, cooperative societies and other large lenders have played an important role in provision refinance facility to MFIs. Banks have also leveraged the Self-Help Group channel to provide direct credit to group borrowers.

INTRODUCTION TO MICROFINANCE:

"Microfinance is the provision of financial services to low-income clients or solidarity lending groups including consumers and the self-employed, who traditionally lack access to banking and related services."

Microfinance is not just about giving micro credit to the poor rather it is an economic development tool whose objective is to assist poor to work their way out of poverty. It covers a wide range of services like credit, savings, insurance, remittance and also non-financial services like training, counseling etc.

SALIENT FEATURES OF MICROFINANCE

Borrowers are from the low income group

Loans are of small amount-micro loans

Short duration loans

Loans are offered without collaterals

High frequency of repayment

Loans are generally taken for income generation purpose

Gaps in financial system and need for microfinance

NEED OF THE STUDY

1**.** The need of microfinance arises because the rural india requires sources of finance for poverty alleviation, procurement of agricultural and farms input.

2. As we know that India is agriculture based economy so microfinance may be a tools to empower the farmers and rural peoples to make agriculture profitable.

3. So the researchers are interested to find out the scopes of microfinance in rural India. This research paper is highlighting a picture rural India as a profitable segment for microfinance institutions.

OBJECTIVES OF THE STUDY

1. To analyze the growth of microfinance sector developed in India and see potential for the microfinance institutions, NGOs, SHGs in the market.

2. To analyze the structure and pattern of microfinance programme in rural Indian by the MFIs, NBFCs.

3. To study the importance and role of microfinance in poverty reduction and profitable agriculture activities.

RESEARCH METHODOLOGY

This is a descriptive research paper based on secondary data. Data have been taken from different websites, research paper and magazines.

CHANNELS OF MICRO FINANCE

In India microfinance operates through two channels:

1. SHG-Bank Linkage Programme (SBLP)

2. Micro Finance Institutions (MFIs)

SHG-BANK LINKAGE PROGRAMME

This is the bank led microfinance channel which was initiated by BABARD in 1992. Under the SHG model the members, usually women in villages are encouraged to form groups of around 10-15. The members contribute their savings in the group periodically and from these savings small loans are provided to the members. In the later period these SHGs are provided with bank loans generally for income generation purpose. The group's members meet periodically when the new savings come in, recovery of past loans are made from the members and also new loans are disbursed. This model has been very much successful in the past and with time it is becoming more popular. The SHGs are self sustaining and once the group becomes stable it starts working on its own with some support from NGOs.

MICRO FINANCE INSTITUTIONS

Those institutions which have microfinance as their main operation are known as micro finance institutions. A number of organizations with varied size and legal forms offer microfinance service. These institutions lend through the concept of joint liability group. A joint liability group is an informal group comprising of 5 to 10 individual members who come together for the purpose of availing bank loans either individually or through the group mechanism against a mutual guarantee. The reason for existence of separate institutions i.e., MFIs for offering microfinance are as follows:

High transaction cost-generally micro credits fall below the break-even point of providing loans by banks.

Absence of collaterals-the poor usually are not in a state to offer collaterals to secure the credit.

Loans are generally taken very short duration periods.

Higher frequency of repayment of installments and higher rate of Default.

Non-Banking Financial Companies, Co-operative societies, Section-25 companies, Societies and Trusts, all such institutions operating in microfinance sector constitute MFIs and together they account for about 42% of the microfinance sector in terms of loans portfolio. The MFI channel is dominated by NBFCs which cover more than 80% of the total loan portfolio through the MFI channel.

TYPES OF MF PROVIDERS

Different legal forms under which MF can be provided in India are:

Societies Registration Act, 1860

NGOs are mostly registered under the Societies Registration Act, 1860. Since these entities were established as voluntary, not-for-profit development organizations, their microfinance activities were also establishment under the same legal umbrella, main purposes is:

1. Relief of poverty

2. Advancement of education

3. Advancement of religion

4. Purpose beneficial to the community or a section of the community.

Indian Trusts Acts, 1882:

Some MFIs are registered under the Indian Trust Act, 1882 either as public charitable trusts or as private, determinable trusts with specified beneficiaries/members.

Not-For-Profit Companies Registered under Section 25 of companies act, 1956:

An organization given a license under section 25 of the companies act 1956 is allowed to be some of the provisions of the companies act, 1956.

Companies Act 1956

For companies that are already registered under the companies act, 1956, if the central government is satisfied that the objects of that company are restricted to the promotion of commerce, science, art, religion, charity or any other useful purpose; and the constitution of such company provides for the application of funds or other income in promoting these objects and prohibits payment of any dividend to its members, then it may allow such a company to register under section 25 of the companies act.

A profile of Rural India

1.350 million Below poverty line

2.95% have no access to microfinance.

3.56%people still borrow from informal sources.

4.70% don’t have any deposit account.

5. 87% no access to credit from formal sources.

6. Annual credit demand is about Rs. 70,000 crores.

7. 95% of the households are without any kind of insurance.

8. Informally Microfinance has been in practice for ages.

INDIAN MICROFINANCE SECTOR

Indian microfinance sector is expected to grow nearly ten times by 2011 to a size of about Rs. 250 billion from the current market size of Rs. 27 billion, at a compounded annual growth rate of 76%. Microfinance in India started evolving in the early 1980s with the formation of informal self help group for providing access to financial services to the needy prople who are deprived of credit facilities. NABARD the regulator for microfinance sector, and small industries development bank of Indian are devoting their financial resources and time towards the developments of microfinance.

One of the fastest growing sectors of India, microfinance is spearheading intense competition among the largest players. By the end of March 2009, microfinance institutions expanded their outreach to 50 million households and about 38 million borrowers.

State wise position of MFIs state wise position of MFIs

State	No. of MFIs	share %
Andhra Pradesh	484	62
Bihar	44	06
Gujarat	08	01
Jharkhand	01	00
Karnataka	20	03
Kerala	14	02
Madhya Pradesh	15	02
Maharashtra	15	02
Orissa	28	04
Rajasthan	18	02
Tamil Nadu	101	13
Uttar Pradesh	05	01
West Bengal	30	04

ROLE OF MICRO FINANCE INSTITUTIONS

1. Poverty reduction tool

Microfinance can be a critical element of an effective poverty reduction strategy. Improved access and efficient provision of savings, credit, and insurance facilities in particular can enable the poor to smooth their consumption, manage their risks better, build their assets gradually, and develop their microenterprises. Microfinance is only a means and not an end. The ultimate goal is to reduce poverty. Government, NGOs and other financial institutions have introduced various welfare schemes and activities to reduce poverty. Microfinance, by providing small loans and savings facilities to those who are excluded from commercial financial services has been developed as a key strategy for reducing poverty throughout the world.

2. Women empowerment

In the rural areas women living below the poverty line are unable to realize their potential. Microfinance programmes are currently being promoted as a key strategy for simultaneously addressing both poverty alleviation and women’s empowerment. The self help groups of women as sources of microfinance have helped them to take part in development activities. The participation of women in self help groups made a significant impact on their empowerment both in social and economic aspects. Vast sections of the rural poor are even now deprived of the basic amenities, opportunities and oppressed by social nongovernment organizations of uplift them both economically and socially. It has been an accepted premise that women were not given enough opportunities to involve themselves in the decision making process of the family as well as in the society. Hence, women were the main target groups under self help groups programme. Microfinance can provide an effective way to assist and empower poor women, who make up a significant proportion of the poor and suffer disproportionately from poverty.

3. Development of the overall financial system

Without permanent access to institutional microfinance, most poor households continue to rely on meager self-finance or informal sources of microfinance, which limits their ability to actively participate in and benefit from the development opportunities. Microfinance can contribute to the development of the overall financial system through integration of financial markets. Microfinance institutions can be small and medium enterprises at the heart of rural sustainable development. Their development positively correlates with rural business development.

4. Self-employment

Poverty reduction through self employment has long been a high priority for the government of India. Microfinance is an experimental tool in its overall strategies. Most of the poor people manage to optimize resources over a time to develop their enterprises. Financial services could enable the poor to leverage their initiative, accelerating the process of generating incomes, assets and economic security. However, conventional finance institutions seldom lend down market to serve the needs of low income families and women headed households. Therefore, fundamental approach is to create the self employment by financing the rural poor through financial institutions. Microfinance, thus, creates the hope and increases the self esteem of the poor by giving the opportunities to be employed.

5. SHG-bank linkage programme

Indian microfinance is dominated by the operational approach self help groups. The approach is popularity known as SHG-Bank linkage model. This model is the dominant model, initiated by the NABARD in the early 1990s. Today the SHG model also links the informal groups of women to the mainstream system and it has the largest outreach to micro financial clients in the world. SHGs comprise a group of 15-20 members. The groups begin by savings that are placed in a common fund. In a way, SHGs are co-operative societies linked to a commercial bank rather than an apex cooperative bank. Once linked to the bank, the SHGs may access a given multiple to the pooled savings for disbursement to its members. The SHG-bank linkage programme was conceived with the objectives of supplementary credit delivery services for the un-reached poor, building mutual trust and confidence between the bankers and the poor and encouraging banking activity both on thrift as well as credit and sustaining a simple and formal mechanism of banking with the poor. The linkage programme combines the flexibility, sensitivity and responsiveness of the informal credit system with the technical and administrative capabilities and financial resources of the formal financial sector which rely heavily on collective strength of the poor, closeness of effective social mobilization functions contributing to an overall empowerment process.

MAJOR INITIATIVES OF GOVERNMENT OF INDIA

There are so many schemes for the upliftment of poor in India. One of them micro credit programmes is run primarily by NABARD in the field of agriculture and SIDBI in the field of industry service and business. The success of micro-credit programme lies in diversification of services. Micro finance scheme of SIDBI is under operation since January, 1999 with a corpus of Rs. 100 crore and a network of about 190 capacity assessed rated MFIs/NGOs. Under the programme, total amount of Rs. 191 crore have been sanctioned upto 31st December, 2003, benefiting over 9 lakh beneficiaries. Under the programme, NGOs/MFIs are supposed to provide equity support because of their poor financial condition. The problem has got aggravated due to declining interest rate on deposit. The office of the development commissionaire (Small Scale Industries) under the ministry of SSI in launching a new scheme of micro finance programme to overcome the constraints in the existing scheme of SIDBI, whose reach is currently very low. It is felt that government role can be critical in expanding reach of the scheme, ensuring long term sustainability of NGOs/MFIs and development of intermediaries for identification of viable projects.

SALIENT FEATURES OF MICRO FINANCE PROGRAMME OF GOVERNMENT OF INDIA:

1. Arranging Fixed Deposit for MFIs/NGOs: Under the scheme government of India arrange money to MFI/NGO like SIDBI for micro credit to poor.

2. Training and Studies on Micro-Finance Programme: Government of India would help SIDBI in meeting the training needs of NGOs, SHGs, intermediaries and entrepreneurs and also in enhancing awareness about the programme. Institutions building for intermediaries for identification of viable projects; the government of India would help in institution building through identification and development of intermediary organization, which would help the NGOs/SHGs in identification of product, preparation of project report, working out forward and back ward linkages and in fixing marketing technology tie-ups. The SISIs would

help in the identification of such intermediaries in different areas.

3. Budgetary Provision for the Scheme During 10th Plan: There was a budgetary provision in 10th five year plan and hoping more funds in next plan.

4. Administrative arrangement: A committee has been formed to control and monitor the administrative arrangement of MFI/NGOs.

CONCLUSION

Microcredit and microfinance have received extensive recognition as a strategy for poverty redaction and for economic empowerment. Microfinance is a way for fighting poverty, particularly in rural areas, where most of the world's poorest live. Accessing small amounts of credit at reasonable interest rates give poor people an opportunity to set up their own small business.

Microfinance has proven to be an effective and powerful tool for rural development and poverty reduction. Like many other development tools, it has sufficiently penetrated the poorer strata of society. The poorest form the vast majority of those without access to microfinance. In India, the micro finance movement has almost assumed the shape of an industry, embracing thousands of NGOs/MFIs. During the last decade, the sector has witnessed a sharp growth with the emergence of a number of micro finance institutions providing financial and non financial supports to the poor in an effort to lift them out of poverty available much needed micro credit to the poor section of the society for generating the self employment.

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